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No. 809

IN THE

Supreme Court of the United States

OCTOBER TERM, 1959

PAUL E. KERN, JEROME PRINCE and CHARLOTTE HEINE,

Petitioners,

vs.

THE COLUMBIA GAS SYSTEM, INC., *et al.*,

Respondents.

BRIEF OF THE COLUMBIA GAS SYSTEM, INC. IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

ON PETITION FOR WRIT OF CERTIORARI

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April 19, 1960

INDEX

PAGE

TABLE OF AUTHORITIES iii

DEFINITIONS AND REFERENCES v

COUNTERSTATEMENT OF QUESTIONS PRESENTED 1

COUNTERSTATEMENT OF THE CASE 2

I. Introduction 2

II. Events Prior to the Post-bankruptcy Interest Decisions (1930-1951) 3

III. The First and Second Post-bankruptcy Interest Decisions (1956-1960) 6

IV. The Third Post-bankruptcy Interest Decision (the Decision Below) 9

SUMMARY OF ARGUMENT 10

ARGUMENT 11

I. NO IMPORTANT QUESTION OF FEDERAL LAW IS PRESENTED BY THE DECISION OF THE COURT OF APPEALS, REAFFIRMING ITS 1957 AND 1959 DECISIONS, THAT UNSECURED CREDITORS OF THE DEBTOR KENTUCKY ARE NOT ENTITLED TO POST-BANKRUPTCY INTEREST FROM THE ASSETS OF THE DEBTOR INLAND 11

A. The Court of Appeals has determined that the Kern proposals, in claiming post-bankruptcy interest for Kentucky creditors out of Inland assets, were contrary to its 1957 and 1959 decisions, and that the District Court properly rejected them for this reason 11

B. Adherence by the Court of Appeals to its 1957 and 1959 decisions raises no important questions of Federal law 14

PAGE

C. Adherence by the Court of Appeals to its 1957 and 1959 decisions involves no "windfall" to Columbia 16

D. Adherence by the Court of Appeals to its 1957 and 1959 decisions is not in conflict with the decision of this Court in *American Iron and Steel Mfg. Co.* v. *Seaboard Air Line Ry.*, 233 U. S. 261 17

II. The Ruling of the Court of Appeals That It Was Not An Abuse of Discretion for the District Court to Refuse to Begin New Plan Proceedings on the Kern Proposals (A) Does Not Present Any Important Question of Federal Law, and (B) Does Not Conflict with the Decision of the Second Circuit in *Knight* v. *Wertheim* 20

A. Refusal to begin new plan proceedings on the Kern proposals does not present any important question of Federal law 20

1. The principle applied by the courts below 21

2. The Trustees' Plan and the Kern proposals 24

3. Petitioners' contentions 28

B. Refusal to begin new plan proceedings on the Kern proposals does not conflict with the decision of the Second Circuit in *Knight* v. *Wertheim* 30

1. The facts in *Knight* 30

2. The decision in *Knight* 32

Conclusion 34

Appendix—Some Comments on Petitioners' Appendix C (Excerpts from Address by J. Arnold Pines, Chief Financial Analyst, Division of Corporate Regulation, Securities and Exchange Commission)

TABLE OF AUTHORITIES

Statutes: PAGE

Bankruptcy Act:

§ 169, 52 Stat. 890 (1938), 11 U. S. C. § 569 (1952) 22

§ 172, 52 Stat. 890 (1938), 11 U. S. C. § 572 (1952) 23

§ 173, 52 Stat. 891 (1938), 11 U. S. C. § 573 (1952) 23

§ 174, 52 Stat. 891 (1938), 11 U. S. C. § 574 (1952) 23

§ 175, 52 Stat. 891 (1938), 11 U. S. C. § 575 23

§ 179, 52 Stat. 892 (1938), 11 U. S. C. § 679 (1952) 23

§ 180, 52 Stat. 892 (1938), 11 U. S. C. § 580 (1952) 23

§ 216, 52 Stat. 895 (1938), 11 U. S. C. § 616 23

§ 221, 52 Stat. 897 (1938), 11 U. S. C. § 621 (1952) 23

§ 222, 52 Stat. 898 (1938), 11 U. S. C. § 622 (1952) 20

§ 224, 52 Stat. 898 (1938), 11 U. S. C. § 624 (1952) 23

§ 229, 66 Stat. 431 (1952), 11 U. S. C. § 629 (1952) 28, 29

PAGE

Judicial Decisions:

American Iron and Steel Mfg. Co. v. Seaboard Air Line Ry., 233 U. S. 261 (1914) 15, 17, 18, 19

Columbia Gas & Electric Corp. v. United States, 151 F. 2d 461 (6th Cir. 1945) *reh. denied*, 153 F. 2d 101, *cert. denied*, 329 U. S. 737 (1946) 4

Country Life Apartments, Inc. v. Buckley, 145 F. 2d 935 (2d Cir. 1944) 21, 28

Ecker v. Western Pacific RR., 318 U. S. 448 (1943) 5

Equitable Office Bldg. Corp., In re, 72 Sup. Ct. 1086 (In Chambers, 1946) 33-34

Group of Institutional Investors v. Chicago, Milwaukee, St. Paul & Pacific R. R., 318 U. S. 523 (1943) 5

Inland Gas Corp., In re, 262 F. 2d 510 (6th Cir.), cert. denied, 359 U. S. 979 (1959) 8

Inland Gas Corp., In re, 241 F. 2d 374 (6th Cir.), cert. denied, 355 U. S. 837 (1957) 7

Inland Gas Corp., In re, 217 F. 2d 207 (6th Cir. 1954) 6

Inland Gas Corp., In re, 211 F. 2d 381 (6th Cir. 1954) 4, 6

Inland Gas Corp., In re, 208 F. 2d 13 (6th Cir. 1953) 6

Inland Gas Corp., In re, 187 F. 2d 813 (6th Cir. 1951) 4

Knight v. Wertheim & Co., 158 F. 2d 838 (2d Cir. 1946) 21, 28, 30-34

Prudence-Bonds Corp. v. City Bank Farmers Trust Co., 186 F. 2d 525 (2d Cir. 1951) 22, 28

R. F. C. v. Denver & Rio Grande Western R. R. Co., 328 U. S. 495 (1946) 5

Other Authorities:

2 Blackstone, Commentaries, p. *488 18

6 Collier, Bankruptcy (14th Ed.) pp. 3898-3899 28-29

House Report No. 2320, 82nd Con., 2d Sess. (1952) 29-30

DEFINITIONS AND REFERENCES

American, Inland and Kentucky: Respectively, American Fuel & Power Company, Inland Gas Corporation and Kentucky Fuel Gas Corporation, the debtors in the three proceedings under Chapter X* of the Bankruptcy Act in the District Court for the Eastern District of Kentucky.

Kern proposals: the "Alterations and Modification of Plan of Reorganization Dated February 25, 1958, as Amended" proposed by Petitioners in the District Court on May 15, 1959.

post-bankruptcy interest: Interest after the institution of a receivership, bankruptcy or reorganization proceeding.

Trustees' Plan: The plan of reorganization for the Debtors filed in the District Court by their Trustees on February 25, 1958, which the District Court confirmed on June 2, 1958, and on June 1, 1959 ordered consummated.

The appendices to the Petition are cited as "Pet. App. "; the appendix to the brief filed by Petitioners in the Court of Appeals as "Kern App "; and the appendix to the brief filed by Columbia in the Court of Appeals as "App. ".

Citations to the opinions below are to the reproduction thereof contained in Appendix B to the Petition.

Emphasis has been supplied to quotations in which emphasis appears.

*The various Chapters and Sections of the Bankruptcy Act are fully cited in the Table of Authorities and are referred to herein only by original Chapter or Section numbers.

COUNTERSTATEMENT OF QUESTIONS PRESENTED

Petitioners state two "Questions Presented", the first relating to procedures under Chapter X of the Bankruptcy Act for the consideration of reorganization proposals, and the second relating to the asserted substantive right on which Petitioners based their reorganization proposals. Since no question relating to Chapter X procedures is presented if, as the Court below held, Petitioners do not have the substantive right on which they based their proposals, we would reverse the order of the "Questions Presented" and restate them as follows:

1. Substantive Right

The Court of Appeals in 1957 determined that the equitable claims of creditors of the Debtor *Kentucky* against the assets of the affiliated Debtor *Inland* do not include post-bankruptcy interest, and reaffirmed that decision in 1959 on appeals from an order confirming a Trustees' Plan expressly based thereon. Did the Court of Appeals err in 1960 by adhering to these decisions and affirming an order of the District Court which (i) rejected reorganization proposals which would have provided for post-bankruptcy interest to creditors of Kentucky from Inland assets and (ii) directed consummation of the Trustees' Plan?

2. Chapter X Procedures

Did the District Court abuse its discretion by refusing to begin new proceedings with respect to reorganization proposals which, although purporting to be an "alteration" of the confirmed Trustees' Plan, provided for a reorganization based on different principles of creditors' rights and a new valuation, to be financed by changed methods and to be carried out by different procedures?

COUNTERSTATEMENT OF THE CASE

I. Introduction

This petition for certiorari is the third attempt by Petitioner Kern to obtain review of rulings by the Court of Appeals that the equitable rights of unsecured creditors of one of the Debtors (Kentucky) do not include a right to post-bankruptcy interest out of the assets of another of the Debtors (Inland):

(i) In February, 1957, upon appeals by Petitioner Kern, the Trustee of Inland and Kentucky and others, the Court of Appeals affirmed an order of the District Court which refused to allow the payment from assets of Inland of post-bankruptcy interest to creditors of Kentucky, and directed the Trustees to prepare and submit for proceedings under Chapter X a reorganization plan in conformity with that ruling. This Court denied petitions for certiorari (including one filed by Petitioner Kern) to review that decision.

(ii) In January, 1959, the Court of Appeals affirmed an order of the District Court confirming a Trustees' Plan which provides that post-bankruptcy interest is not to be paid to unsecured creditors of Kentucky. This Court denied petitions for certiorari (including one filed by Petitioner Kern) to review that decision.

(iii) In January, 1960, the Court of Appeals affirmed an order of the District Court which refused to start plan proceedings upon reorganization proposals offered by Kern providing for post-bankruptcy interest from the assets of Inland to the unsecured creditors of Kentucky, and directed that the confirmed Trustees' Plan be carried out forthwith. This is the decision of which the present Petition seeks review.

We respectfully refer the Court to the briefs which we filed in connection with Kern's petitions for certiorari referred to above.* In the Counterstatement which follows, we review briefly the facts and prior proceedings which bear on the questions presented by the Petition.

II. Events Prior to the Post-bankruptcy Interest Decisions

1930-1951

1. These three proceedings in Chapter X relate to three Debtors affiliated by stock ownership. One of the Debtors (Inland) owns all the operating assets. Of the other two Debtors, American owns 72.6% and Kentucky 26% of Inland's capital stock. Kentucky has no other assets. The Petitioners are creditors of Kentucky.

2. Each proceeding began as an equity receivership (Inland and Kentucky in 1930; American in 1934); continued as a proceeding under former Section 77B of the Bankruptcy Act during the entire operating life of that statute, and each has continued as a proceeding in Chapter X during the entire life to date of that statute.

3. Each of the Debtors had outstanding, when proceedings were instituted, large amounts of debt securities. Part of the debt securities of each Debtor were publicly held and part of each were owned by Columbia. Columbia owns now what it owned when the proceedings were instituted; the publicly held securities have been widely and actively traded during the period of the proceedings.

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*Consolidated Brief in Opposition to Petitions Nos. 325, 336 and 342 (October Term, 1957); Consolidated Brief in Opposition to Petitions Nos. 756, 766 and 774 (October Term, 1958) and the Memorandum in Reply to the Securities and Exchange Commission in such cases.

4. In 1945, the Court of Appeals held that, for equitable reasons, Columbia's claims against each of the Debtors should be subordinated to the claims of the public creditors of that Debtor. Columbia had strongly, but unsuccessfully, contended both before the District Court and the Court of Appeals, both as to the asserted facts and as to the law, that this subordination was not justified. Columbia petitioned this Court, on the points of law involved, for certiorari, which this Court denied.*

5. Thereafter, in plan proceedings before the District Court, it became apparent that Inland's assets would be sufficient to pay all its own public creditors in full and leave a surplus of Inland's assets for Columbia's subordinated claims against Inland. The District Court approved a plan recognizing such a recovery for Columbia, but the Court of Appeals reversed (in 1951) and granted further equitable relief to the public creditors of American and Kentucky. It did so by holding that, in equity, such creditors should be treated as "quasi-creditors" of Inland and that the surplus Inland assets should be allocated to the payment of their claims in proportion to the respective stock interests of their own Debtors in Inland (72.6% American, 26% Kentucky).**

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*_Columbia Gas & Electric Corp. v. United States_, 151 F. 2d 461 (6th Cir. 1945), _cert. denied_, 329 U. S. 737.

The statement in the Petition (p. 3, n. 1) that this decision subordinated Columbia's claims against each of the Debtors to the claims of all other creditors "in the System" is a fantasy of Petitioners. The three proceedings were not consolidated, three separate appeals were taken and a separate mandate subordinating Columbia's claims was entered in each of the three proceedings. The Court of Appeals has been emphatic that it would not treat the Debtors as a single economic entity with creditors of each treated as though they were creditors of that single entity. See, for instance, _In re Inland Gas Corp._, 211 F. 2d 381, 383 (6th Cir. 1954).

**_In re Inland Gas Corp._, 187 F. 2d 813 (6th Cir. 1951).

6. Columbia had strongly contested this additional grant of equitable relief to public creditors of American and Kentucky. However, believing that that decision (although adverse to it) opened the way for a prompt reorganization of the Debtors, Columbia did not petition for certiorari, and for the next five years (1951-1956) participated in District Court proceedings only as observer and did not participate in any of the appeals during that period.

1951-1956

7. The hope of prompt reorganization proved illusory. With Columbia on the sidelines, the diligent efforts of the District Court and the Trustees to accomplish a reorganization were thwarted by continuous internecine warfare among the public holders of various securities of Kentucky and American and their representatives.* Aspects

*Kern praises the longevity of these proceedings for resulting in "the highest achievement attainable under the Bankruptcy Act" (Pet. p. 3)—payment of many of the Debtors' securities issues in full—which he likens to a series of "piecemeal" reorganizations. We doubt that this atomization of the reorganization process over 30 years constitutes the "highest achievement" attainable under the Bankruptcy Act". *Cf. Ecker* v. *Western Pacific R. R.*, 318 U. S. 448, 508-509 (1943); *Group of Institutional Investors* v. *Chicago, Milwaukee, St. Paul & Pacific R. R.*, 318 U. S. 523, 542-546 (1942); *RFC* v. *Denver & Rio Grande Western R. R.*, 328 U. S. 495, 520-524 (1946). In the *Milwaukee* case this Court made a statement (318 U. S. 523, 545) which we believe applicable to Chapter X:

> "... Nor can we conclude that there is anything in § 77 which indicates that it may be used *merely as a moratorium*. ... We cannot conclude that in this proceeding, which already has been pending *seven* years and which was before the Commission for over *four* years, the interests of junior claimants have been sacrificed for speed. ..."

Furthermore, the length of these proceedings is not a reflection of the customary judicial dilemma in depression era reorganizations arising from the fact that prompt reorganization precludes recognition of junior interests at a time of abnormally depressed values while delayed reorganization prejudices the rights of senior interests. The past decade of these proceedings (all years of prosperity and high value) reflect not such a judicial dilemma but persistent and unmeri-

of such litigation are reflected in the opinions of the Court of Appeals in *In re Inland Gas Corp.*, 208 F. 2d 13 (6th Cir. 1953), *In re Inland Gas Corporation*, 211 F. 2d 381 (6th Cir. 1954) and *In re Inland Gas Corp.*, 217 F. 2d 207 (6th Cir. 1954).

8. During this five-year period in which Columbia did not participate, the Court of Appeals gave further equitable relief to public holders of Kentucky Bonds. By 1954 it was apparent that the 72.6% of the excess Inland assets which the Court had allocated to American public creditors in 1951 (see par. 5 above) would more than suffice to pay full principal and interest on their secured claims. At the urging of Kentucky creditors, the Court of Appeals held that the excess of the American creditors' 72.6% quasi-creditor share of Inland assets should be applied to the claims of the public holders of Kentucky Bonds.*

III. The First and Second Post-bankruptcy Interest Decisions

1956-1960

9. The District Court on March 14, 1956, entered the order described in sub-paragraph (i), p. 2, above. On the appeals from this order, Columbia participated as appellee. The Court of Appeals affirmed, one judge dissenting. The Court in its opinion expressly asserted that it could, in effect, award post-bankruptcy interest to Kentucky creditors from Inland's assets by a complete rejection of Columbia's claims,

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torious litigation by Kern. Commencing with his acquisition of 34% of the Kentucky bond issue, he has generated controversy after controversy in the District Court and, after adverse decision, assiduously pursued his appellate remedies (six appeals in the past seven years, all found to be without merit and several found to be attempts to relitigate prior decisions of the Court of Appeals).

In re Inland Gas Corp., 211 F. 2d 381 (6th Cir. 1954).

but declined to exercise that authority. This Court denied certiorari.*

10. The Trustees, pursuant to the direction of the District Court's order so affirmed, prepared and filed in February, 1958 the Trustees' Plan here involved. That Plan states as one of the "Principles Governing Reorganization", that:

> "In compliance with the latest decision of the Court of Appeals in the Proceedings, the quasi-creditor claims against Inland of the holders, other than Columbia, of Kentucky Bonds and Debentures do not include Post-bankruptcy Interest."

On the basis of that principle, the Trustees' Plan provides for payment to public creditors of Kentucky from the assets of Inland of full principal and pre-bankruptcy interest, but no post-bankruptcy interest from such assets.**

Hearings on the Trustees' Plan were held through the spring of 1958. The District Court received expert testimony and other evidence in support of the valuation of the Debtors' properties (derived from estimates of future earnings) on which the Plan is based. Petitioner Kern filed voluminous objections and proposed amendments to the Plan. He also criticized the Plan valuation as inadequate and, in support of that criticism, sponsored witnesses who testified that, under stock market conditions then extant, there could be sold at par an amount of stock in the reorganized company which was much greater than the amount of stock which the Plan provided for distribution on creditor claims.

11. By various orders culminating in an order entered June 2, 1958, confirming the Plan, the District Court (1)

In re Inland Gas Corp., 241 F. 2d 374 (6th Cir. 1957), *cert. denied*, 355 U. S. 837.

**A summary of the principal provisions of the Trustees' Plan appears at pp. 24-26 of this Brief.

determined that the valuation of the Debtors set forth in the Plan is fair, (2) determined that each of the Debtors is insolvent, and (3) found that the Plan is fair, equitable and feasible and in compliance with all applicable provisions of the Bankruptcy Act.

12. Petitioner Kern appealed from the order confirming the Trustees' Plan. He urged that the Court of Appeals repudiate its 1957 decision; that the District Court had misunderstood and misapplied the principles of that decision; and that the District Court was wrong in adopting the Trustees', and not Kern's, valuation method and valuation figure. On January 15, 1959, the Court of Appeals dismissed his appeal. In so doing, it said:

> "... [W]e find that the district judge exercised sound discretion in adopting the evaluation which he did, upon the basis of the expert evidence before him."

The Court of Appeals then found that the principles stated in its 1957 decision had been correctly applied and were dispositive of all Kern's other contentions. The Court, in a unanimous opinion, said:

> "... It is obvious that the district judge attempted to the best of his ability and understanding —and we think successfully—to apply the principles stated in our last opinion [241 F. (2d) 374] and to put into full effect the mandate of this court. ...
>
> "We are of opinion, further, that Judge Ford appropriately applied the adjudication of this court in 241 F. (2d) 374, with respect to post-bankruptcy interest and all other issues before him. ..."*

Kern's petition for certiorari was denied on April 27, 1959.**

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*262 F. 2d 510, 511.
**359 U. S. 979.

IV. The Third Post-bankruptcy Interest Decision (the Decision Below).

13. Upon denial of certiorari to the *second* post-bankruptcy interest decision (i) the Trustees petitioned the District Court for an order to aid consummation of their Plan* and (ii) Kern *et al.* brought forward their petition to "alter" the confirmed Plan as provided in their proposals (denominated "Alterations and Modifications").

These proposals would have provided the Kentucky creditors a recovery, from Inland assets, on account of post-bankruptcy interest on their claims against Kentucky. To accomplish this end the proposals would have changed every operative provision of the Trustees' Plan.**

14. The District Court received memoranda and heard argument for a full court day; on the following day, stating that he had reached his decision "after having considered the entire picture of our problem", the Judge refused to begin new proceedings on the Kern proposals and directed prompt consummation of the confirmed Trustees' Plan. The Court of Appeals affirmed.

One ground of the District Court's decision, and one ground of the decision of the Court of Appeals affirming it, was the conclusion that the Kern proposals were an attempt to relitigate the 1957 and 1959 decisions of the Court of Appeals that the unsecured Kentucky creditors are not entitled to post-bankruptcy interest from the Inland estate.

Both courts also expressly based their decisions on the grounds that the Kern proposals in substance were a new

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*The Trustees' Plan provides that it shall be carried out as soon as practicable after the confirmation order has become final and not subject to further review.

**A summary of the principal changes in the Trustees' Plan proposed by Petitioners appears at pp. 26-28 of this Brief.

plan and not an "alteration" or a "modification" of the confirmed Trustees' Plan, the Court of Appeals stating that the District Court did not abuse its discretion in so finding them and in refusing to begin new plan proceedings.

SUMMARY OF ARGUMENT

The Court of Appeals has determined that these proceedings should be terminated by consummation of the confirmed Trustees' Plan, and that new proceedings with respect to the Kern proposals should not be commenced. Its decision rests on grounds which clearly are right and which present no question which should be reviewed by this Court.

The Kern proposals were based upon an asserted "quasi-creditor" right of *Kentucky* creditors to recover post-bankruptcy interest from the assets of *Inland*. Twice prior to the decision below, the Court of Appeals had determined that the "quasi-creditor" rights, which *it* had conferred on Kentucky creditors, do *not* include post-bankruptcy interest. It has so ruled for the third time. No important question of Federal law is presented by its decision so reaffirming the scope of equitable rights created by it. The arguments by Petitioners that the Court of Appeals ought to have departed from its prior decisions—one based on an asserted "windfall" which Columbia would otherwise derive, and the other based on an asserted "solvency" of Inland (not *Kentucky*)—are without substance.

The Court of Appeals also was right in holding that the District Court did not abuse its discretion in refusing to begin new proceedings on the Kern proposals. The statute makes plain, and judicial decisions confirm, that proposals to "alter" a confirmed plan are addressed to the discretion of the Court, which should not be exercised in favor of proposals which are in substance a new plan. The Kern proposals would have eliminated or substantially changed

every operative provision of the Trustees' Plan, including its valuation and findings that all the Debtors are insolvent; its principles of creditor participation; its method of financing reorganization and its detailed procedures for consummation. The decision, upon exercise of discretion, that such proposals were a new plan presents no question which this Court should review. Petitioners' argument that the decision conflicts with the Second Circuit's ruling in *Knight* v. *Wertheim* is without merit, since the Court in *Knight* applied the same principles as the Court of Appeals, and expressly found that the limited plan changes there involved were not a new plan.

The Petition should be denied.

ARGUMENT

I.

NO IMPORTANT QUESTION OF FEDERAL LAW IS PRESENTED BY THE DECISION OF THE COURT OF APPEALS, REAFFIRMING ITS 1957 AND 1959 DECISIONS, THAT UNSECURED CREDITORS OF THE DEBTOR KENTUCKY ARE NOT ENTITLED TO POSTBANKRUPTCY INTEREST FROM THE ASSETS OF THE DEBTOR INLAND.

A. The Court of Appeals Has Determined that the Kern Proposals, in Claiming Post-bankruptcy Interest for Kentucky Creditors out of Inland Assets, Were Contrary to its 1957 and 1959 Decisions, and that the District Court Properly Rejected Them for this Reason.

Petitioners' proposals were squarely based on an assumed substantive right of public holders of *Kentucky* securities to the payment of post-bankruptcy interest directly from the assets of *Inland*. If such right did not exist in law or

equity, Petitioners' proposals were properly rejected without regard to the other problems they posed.

No statute or contract gives the creditors of Kentucky any rights against the assets of Inland. Petitioners' asserted right to post-bankruptcy interest from Inland assets depended entirely upon their interpretation of the decisions of the Court of Appeals which created and defined their "quasi-creditor" claim. They contended that such decisions had given them that right. *Contra*, those supporting the Trustees' Plan urged that the 1957 and 1959 decisions of the Court of Appeals had each expressly determined that the quasi-creditor claim given the Kentucky creditors does not include post-bankruptcy interest.

Both the District Court and the Court of Appeals rejected Petitioners' interpretation of the prior decisions of the Court of Appeals and held that the asserted "quasi-creditor" claim for post-bankruptcy interest was non-existent.

The District Court was emphatic to this effect when it said that the Kern proposals were

> "... predicated only upon the assertion of a right on the part of the public holders of Kentucky bonds and debentures which has already been adjudicated adversely to them and to their claims. ... I think that to grant the hearing that is sought upon this proposed substituted Plan would be to clearly disregard the decisions of the Court of Appeals to the effect that these quasi-creditor claims on behalf of Kentucky creditors do not include [post] bankruptcy interest ..."*

Petitioners' appeal from this decision presented the basic question of the existence or non-existence of the substantive right to post-bankruptcy interest from Inland assets asserted in the Kern proposals. The Court of Appeals made crystal

*Transcript of Proceedings, May 28-29, 1959, Kern App. 66a-67a.

clear that it had twice previously decided that such a substantive right did *not* exist and that it was now again reaffirming those decisions. After a summary background statement, that Court stated:

> *As to its 1957 and 1959 decisions*: ". . . our last two opinions, . . . reported respectively at 241 F. 2d 374 (1957) and at 262 F. 2d 510 (1959) relate to, *and we think control*, the issues directly presented by the present appeals." (Pet. App. 5c)
>
> *As to its 1957 decision*: ". . . we held directly that post-bankruptcy interest should not be allowed the public holders of bonds and debentures of the Kentucky Gas and Fuel Corporation." (*id.* at 5c and 6c)
>
> *As to its 1959 decision*: In the opinion ". . . reported at 262 F. 2d 510 . . . we stated that United States District Judge Ford had appropriately applied our adjudication set out in 241 F. 2d 374 [the 1957 decision] with respect to post-bankruptcy interest and to all other issues before him." (*id.* at 5c)
>
> *As to the District Court's action*: ". . . At the conclusion of the hearing, the district judge announced his denial and rejection of the proposed petition for alterations and modifications and granted the petition of the [Trustee of] Inland Gas Corporation for an order consummating the plan . . . *We are of opinion that the United States District Court correctly and faithfully followed the mandate of this court.*" (*id.* at 6c)

Thereafter, plainly in response to the detailed arguments made by the Inland Trustee and Columbia, as appellees, that the asserted quasi-creditor claim for post-bankruptcy interest had been rejected by its 1957 and 1959 decision, the Court of Appeals said:

> "The appellees are correct in their assertion that the proposed "alterations and modifications" consti-

tute an attempt to relitigate matters previously decided by this Court and that the District Judge did not abuse his discretion in denying them consideration" (*id.* at 13c).

B. Adherence by the Court of Appeals to Its 1957 and 1959 Decisions Raises No Important Question of Federal Law.

The decision below, refusing for the third time to create an equitable claim in public creditors of Kentucky for post-bankruptcy interest from the assets of Inland was neither an abuse of discretion nor the source of any important question of federal law. No one can purport to catalogue the equitable considerations which were weighed by the Courts below in initially deciding the question in 1957. But whatever the equitable considerations found decisive at that time, the proceedings conducted in reliance upon that decision and upon the 1959 decision reaffirming it, constitute an additional factor which supports the 1960 decision of the Court of Appeals to adhere to its former decisions.

A plan (the Trustees' Plan) was developed and fully considered on the basis of the 1957 decision. Kern had (and fully utilized) the right to present, prior to confirmation of the Trustees' Plan, his own reorganization proposals. These were rejected by the District Court, which confirmed the Trustees' Plan, and the 1959 decision of the Court of Appeals fully approved the District Court's action upon appeal by Kern. In considering Kern's third appeal on the post-bankruptcy interest question—this time, from the District Court's order to carry out the confirmed and affirmed Trustees' Plan—the Court of Appeals properly could consider the enormous *quanta* of time, effort and money expended toward accomplishment of reorganization on the premise stated in the confirmed Trustees' Plan—that the quasi-creditor claim of the Kentucky creditors does not include post-bankruptcy interest. The decision of the

Court of Appeals to adhere to its 1957 and 1959 decisions under the circumstances clearly was not an abuse of discretion.

The facts of this proceeding are obviously unique and virtually impossible of recurrence; and, for this reason, the decision of the Court of Appeals, inextricably dependent on such facts, does not raise any important question of federal law. Indeed, Petitioner Kern no longer contends that the Court of Appeals misunderstands the rules of law relating to post-bankruptcy interest. This year's certiorari petition is but a renewed complaint against the refusal of the Court of Appeals to grant additional equitable relief to Kentucky creditors. The thrust of the Petition is that the stock underwritings contemplated by the Kern proposals made it necessary to grant such additional equitable relief because

> (i) in view of the value placed by the underwriters on the stock of Inland, refusal to create a quasi-creditor claim for post-bankruptcy interest would result in a "windfall" to Columbia; and
>
> (ii) the proposed underwritings showed that Inland (though not Kentucky) had become "solvent", and under the decision of this Court in the *American Iron and Steel Mfg. Co.** case, creditors of a "solvent" debtor are entitled to post-bankruptcy interest.

Petitioners argued and briefed both these contentions to the Court of Appeals. Neither was found persuasive by the majority of that Court as calling for a departure from its prior decisions. In subdivisions "C" and "D" which follow, we treat briefly the reasons which support the decision below in this regard.

**American Iron and Steel Mfg. Co.* v. *Seaboard Air Line Ry.*, 233 U. S. 261.

C. Adherence by the Court of Appeals to Its 1957 and 1959 Decisions Involves No "Windfall" to Columbia.

The Petition urges that the decision of the Court of Appeals "enables Columbia to escape with a windfall, over and above its allowable claims . . ." (Petition, p. 13). This statement (and others of the same tenor with which the Petition is spiced) are demonstrably false. The record includes a computation made by S. E. C.'s representative in the District Court proceedings, full of assumptions favorable to proving a windfall. Such assumptions included valuing the Inland properties on the basis of the capitalization which the Kern proposals would give the new company. Even using this stock-market valuation, the computation showed that the value of the stock to be issued to Columbia under the Trustees' Plan was then* *less* than the total amount of its claims against the Debtor Inland alone. The computation also showed that if reorganization were to be delayed long enough there would come a point when cash accumulated from Trustee earnings, plus the underwriter's capitalization, would begin to produce a value to Columbia in excess of its claims against Inland.**

*The computation with respect to the alleged "windfall" was presented to the District Court in May, 1959, when the Kern proposals were before that Court. It purported to demonstrate that, by the then future date of August 31, 1959, on the basis of the stock market valuation, the value of the securities going to Columbia under the Trustees' Plan would exceed Columbia's total claims against *Inland* (*i.e.*, not including Columbia's claims against *American* and *Kentucky*) by something less than $200,000. But reversing this very computation and backtracking from the then future August 31 to the May date when it was presented, there was no "windfall" (even on the stock market valuation). The computation appears at pp. 49b-50b of the Appendix to Columbia's Brief in the Court of Appeals, filed as part of the record before this Court.

**The Petition includes as "Appendix C", apparently as material to the "windfall" argument in particular, excerpts from an address by J. Arnold Pines, Chief Financial Analyst, Division of Corporate

But such excess, if any, is in no sense "windfall" to Columbia. Columbia holds large and wholly unsatisfied claims against the Debtors American and Kentucky, which the *Trustees' Plan recognizes as valid and for the participation of which it provides.** Columbia is Inland's junior creditor. If there exist any Inland assets in excess of Columbia's claims against Inland, under normal principles of reorganization law such assets pass into the respective estates of Kentucky and American, in proportion to their ownership of the stock of Inland (26% and 72.6%, respectively); and, as Columbia is the only creditor of either American and Kentucky whose claims for principal have not been satisfied, such assets would then be properly assigned to the payment of its claims against each such Debtor.

D. Adherence By the Court of Appeals to Its 1957 and 1959 Decisions Does Not Conflict With the Decision of this Court in American Iron and Steel Mfg. Co. v. Seaboard Air Line Ry., 233 U. S. 261.

The Petition urges that the decision of the Court of Appeals conflicts with the decision of this Court in the *American Iron and Steel* case in failing to give to Kentucky creditors the benefit of the principle that post-bankruptcy interest should be paid to unsecured creditors if the debtor proves solvent. It is argued that the Kern proposals to pay Columbia's claims against Inland established that Inland is "solvent"; and that as unsecured creditors of a "solvent" debtor, Kentucky creditors were entitled to post-bankruptcy interest from the "solvent" Inland estate under that principle.

Regulation, Securities and Exchange Commission, delivered at the Rutgers University School of Business Administration. We present in the appendix to this brief some comments with respect to the statements made in that address.

*Plan, Art. VI, Sec. 2(a).

An initial and basic failure in this argument is apparent from the discussion above. No possibility of conflict with the decision in *American Iron and Steel* exists if the quasi-creditor claim given Kentucky creditors by the Court of Appeals does not include post-bankruptcy interest whether or not Inland is solvent. Certainly that Court had authority in defining the extent of Kentucky creditor participation in Inland assets as "quasi-creditors", to say that such participation does not include post-bankruptcy interest whether or not *Inland* proves solvent.* The District Court has so understood the Court of Appeals, and the Court of Appeals, for the second time, has said that the District Court correctly and faithfully followed its mandate. Clearly, the decision of the Court of Appeals rests on grounds which preclude any conflict with *American Iron and Steel.*

There are other reasons why rejection of the Kern proposals does not conflict with *American Iron and Steel,* even assuming, contrary to fact, that Kentucky creditors are entitled to post-bankruptcy interest if *Inland* is solvent. We mention one of them here to correct the statement in the Petition that the Kern proposals met the requirements of the "solvency exception". Certainly they did not. The basic and obvious prerequisite to applicability of the "solvency exception" is that the debtor be solvent—that there exist a surplus of assets in excess of *all* claims.** This Court in *American Iron and Steel,* after citing the passage from

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*Apart from the "quasi-creditor" doctrine and under rules of law generally applied, only the solvency of *Kentucky* would give *Kentucky* creditors a basis for claiming the benefits of the "solvency exception". Petitioners do not question the continued and hopeless insolvency of Kentucky.

**As stated in Blackstone:

> ". . . [T]he usual rule is, that all interest on debts carrying interest shall cease from the time of issuing the [receiver's] commission, yet, if case of a surplus left *after payment of every debt,* such interest shall again revive . . ." (2 Blackstone, Commentaries * 488)

Blackstone quoted in the footnote, said that the principle applied "where the assets ultimately prove sufficient to pay *all debts in full*" (233 U. S. at 267). The Kern proposals did not meet this basic requirement. They showed that the funds to make Inland "solvent" by paying Columbia's Inland claims would come in substantial part, not from the "practical offers of hard money", etc. (Petition, p. 8) from underwriters, but from funds held by the Inland Trustee and set aside by the Trustees' Plan for the payment of the reorganization expenses of all the Debtors and for payment of certain other priority claims. In short, the Kern proposals did not provide funds sufficient for the payment of all claims against Inland. They provided funds sufficient to pay Inland's junior creditor (Columbia) by deferring payment of some of Inland's senior creditors. If such proposals proved anything other than Kern's persistence, they proved that, as the Plan states and the courts below determined, Inland is insolvent.

We omit in the interests of brevity a statement of additional reasons why there is no conflict here with *American Iron and Steel* and other decisions which have applied the "solvency exception". One related argument in the Petition, however, deserves brief comment—the argument (Petition, pp. 24-5) that certiorari should be granted in this case because the lower federal courts would be helped by an opinion of this Court defining generally the exceptions to the principle that interest does not accrue after commencement of bankruptcy proceedings. We think this invitation to render an advisory opinion points up sharply Petitioners' lack of decent grounds for certiorari.

II.

THE RULING OF THE COURT OF APPEALS THAT IT WAS NOT AN ABUSE OF DISCRETION FOR THE DISTRICT COURT TO REFUSE TO BEGIN NEW PLAN PROCEEDINGS ON THE KERN PROPOSALS (A) DOES NOT PRESENT ANY IMPORTANT QUESTION OF FEDERAL LAW, AND (B) DOES NOT CONFLICT WITH THE DECISION OF THE SECOND CIRCUIT IN *KNIGHT* v. *WERTHEIM*.

A. Refusal to begin new plan proceedings on the Kern proposals does not present any important question of federal law.

The authority to effect any change in the confirmed Trustees' Plan derives exclusively from Section 222 of the Act. Section 222 provides that a plan may be "altered or modified", after confirmation "with the approval of the judge", and, if the "alteration or modification" is one which "materially and adversely" affects the interests of creditors, after hearings and other proceedings are had with respect to it.* The Kern proposals were offered under Section 222 as an "alteration or modification" of the confirmed Trustees' Plan. It was alleged that the proposals "materially and adversely affect the interests of creditors".** The District

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*Section 222 is quoted in full at Pet. App. 1c.

**Kern Petition for Alterations, etc., para. 8. One creditor adversely affected by the Kern proposals was Columbia, whose claims against American and Kentucky are treated by the confirmed Plan as "entitled to participate". The Kern proposals, as the District Court pointed out, would have treated such claims as "not entitled to participate". This fact, and the fact that Kern himself alleged that his proposals materially and adversely affected creditors, greatly detract from the position of Judge Miller, dissenting below, that the proposals did *not* have such adverse effect and that therefore Judge Ford abused his discretion in refusing to accept them. With the greatest respect for Judge Miller, we submit that his dissenting opinion is based on a misapprehension of Section 222; material and adverse effect is *not* the test for determining whether an "alteration" may be

Court, with which the Court of Appeals agreed, refused to begin the hearings and other proceedings specified in Section 222.

1. The Principle Applied By the Courts Below

The principle applied by both Courts is that proposals to "alter" a confirmed plan are addressed to the discretion of the Court and that sound discretion requires the rejection of proposals which, because of the nature and extent of the changes they require, are in substance a new plan.

The *principle* thus applied to the Kern proposals is abundantly supported by authority: every reported decision under former Section 77B or Chapter X with respect to a proposed "alteration" to a confirmed plan recognizes it. *E.g.*, *Country Life Apartments, Inc.* v. *Buckley*, 145 F. 2d 935 (2d Cir. 1944) (affirming rejection of reorganization proposals found to constitute a new plan):

> "Appellants' proposals . . . . differed so greatly from the trustee's plan that they could not possibly be treated as a mere modification . . ."
>
> ". . . Upon ascertaining this fact, the District Court was not required to listen to further arguments on the merits of the proposals, and hence committed no error in denying appellants further opportunity to be heard." (at p. 937)

Knight v. *Wertheim*, 158 F. 2d 838 (2d Cir. 1946) (reversing rejection of reorganization proposals upon finding that such proposals did *not* constitute a new plan):

> ". . . [T]he order [rejecting a proposed alteration of a confirmed plan] may not be disturbed unless

filed; Section 222 permits the judge, in his discretion, to permit the filing of an "alteration" whether or not it materially and adversely affects security holders; adverse effect is the test of whether or not the judge must hold a hearing upon an alteration "filed with his approval", and start again the series of statutory steps leading to plan approval, acceptance and confirmation.

he overstepped the permissible limits of his discretion. . . . (at p. 841)

". . .

". . . We said in our opinion [in *Country Life, supra*] that there was a limit to what might be considered an 'alteration' or a 'modification' and that the proposal had exceeded it . . .

". . . [T]he proposed changes themselves [were not] so radical as to fall within our decision in Country Life. . . ." (at pp. 842, 843)

Prudence-Bonds Corp. v. *City Bank Farmers Trust Co.*, 186 F. 2d 525 (2d Cir. 1951) (affirming order which approved amendment of plan):

". . . [T]he court may never under the guise of 'alteration' or 'modification' substitute an entirely new 'plan' in place of the original; although what is the line between a substitute and an 'alteration' or a 'modification' is necessarily left at large.

". . .

"The question is one of discretion, though of a discretion which should be sparingly exercised. . . ." (at p. 528)

These authorities, and the decision below, are firmly grounded in the Chapter X scheme, under which there is a regular sequence of steps leading to the confirmation of a plan.* As set forth in the footnote, Chapter X makes

*The sequence of such steps in all cases in which the debtor's indebtedness exceeds $3,000,000, is in summary as follows:

(1) *Trustee's Preparation of a Plan.* The Judge must fix a time within which the trustee shall prepare and file a plan (or a report why a plan cannot be effected) (Sec. 169).

(2) *Hearing on This, and Other, Plans.* The judge must also fix a date for hearing on the trustee's plan, on objections thereto and on "such amendments *or plans* as may be proposed by the debtor or any creditor or stockholder" (Sec. 169).

specific provisions for consideration, prior to confirmation, of plans alternative to the trustee's plan, and does not make District Court approval a prerequisite to the filing of such alternative plans. The Act then provides for confirmation of the one plan which has been accepted by creditors and stockholders, and states that, upon confirmation, "the plan and its provisions shall be binding upon the debtor . . . and upon all creditors and stockholders. . . ." (Section 224(1)). Confirmation does not cut off the authority of the Court to approve even an "alteration" which adversely affects creditors. But after a plan has been developed, accepted by creditors and confirmed, it is for the Court, and not each creditor group, to determine

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(3) *Advisory Report of SEC.* After this hearing, the Judge must submit to SEC for examination and a report (to be advisory only) "the plan *or plans* which [he] regards as worthy of consideration" (Sec. 172).

(4) *Approval of Plan or Plans.* The Judge must not enter an order approving a plan until SEC has filed its report or notified him that it will not file one or until the expiration of such reasonable time as he has fixed (Sec. 173). Thereafter, the Judge "shall enter, an order approving the plan *or plans*" which shall include the Act's required provisions (Sec. 216), and are fair, equitable and feasible (Sec. 174).

(5) *Submission for Acceptance by Affected Creditors and Stockholders.* The Judge must fix a time within which affected creditors and stockholders may accept (Sec. 174), and the trustee must transmit to all affected creditors and stockholders, "*the plan or plans* so approved", the opinion of the Judge approving it or them and the report of SEC (and also, or alternatively, summaries of them), (Sec. 175).

(6) *Confirmation of Plan.* After a plan has been accepted by the required percentages of each class of creditors and stockholders affected by the plan (⅔ for a creditor class, a majority for stockholders) there is to be a hearing for the consideration of the confirmation of the plan and of such objections as may be made to the confirmation (Sec. 179). The prior "approval" order (item 4 above) is not to affect the right of a creditor or stockholder to object to "confirmation" (Sec. 180).

The Judge is to confirm the plan if satisfied that it is fair and equitable and feasible and if satisfied as to other matters enumerated (Sec. 221).

whether *part* of the progress made toward reorganization is to be scrapped by consideration of proposals to "alter" a *provision* of the plan. The plainest considerations of orderly procedure and concern for time and expense strongly urge that the Court's discretion be exercised against scrapping *all* the progress made toward reorganization and embodied in a confirmed plan, by beginning consideration of proposals which in substance are a new plan.

2. The Trustees' Plan and the Kern Proposals

The District Court and the Court of Appeals correctly applied these principles, as comparison of the Trustees' Plan and the Kern proposals plainly reflects.*

The Trustees' Plan is based upon:

(a) a statement of principles governing priority of claims against, and participation in the assets of, the Debtors (set forth in Art. I, Sec. 2, "Principles Governing Reorganization", App. 5b);

(b) a valuation of the Debtors' (principally Inland's) properties and business of $7,199,100 which with Trustees' excess cash (cash not required for reorganization expenses and new company working capital) produced a reorganization value as of December 31, 1957, of $10,538,000 (Art. V, Sec. 3, App. 19b); and

(c) findings that each of the Debtors is insolvent (Art. I, Sec. 2, App. 6b).

*The full extent of such changes in the confirmed Plan proposed by Petitioners appears from the consolidated printing of the confirmed Plan and the Kern proposals included in the appendix to our Brief in the Court of Appeals, filed as part of the record before this Court. Page citations in the comparison above ("App. 5b", etc.) are to such appendix.

The Trustees' Plan provides for:

(d) an unsecured borrowing by the Inland Trustee from Chemical Corn Exchange Bank in the amount of $4,000,000 to provide funds which, with Trustees' cash, will suffice to pay in cash all claims against the Debtors other than Columbia's (Art. VIII, Sec. 2, App. 27b);

(e) the payment by the Trustees of such claims—principally the publicly-held secured American Notes (principal and full interest) and the publicly-held Kentucky Bonds and Debentures (principal and pre-bankruptcy interest only) (Art. VIII, Sec. 3, App. 28b);

(f) the reservation by the Trustees prior to the transfers mentioned in the next subdivision (g), of funds to pay all Class 1 claims against the Debtors (Class 1 claims being so defined as to include amounts which the District Court, prior to confirmation, had ordered paid to public holders of securities of American, Inland and Kentucky, amounts to be distributed under the Plan to public holders of American Notes and Kentucky Bonds and Debentures, and reorganization fees and expenses) (Art. IX, Sec. 4; App. 36b);

(g) the transfer of physical properties and remaining cash balances of the Debtors to a new corporation which would assume the Inland Trustee's liability to Chemical Bank and would issue its stock to an escrow agent, by whom it would be held until Columbia obtains SEC permission under the Public Utility Holding Company Act of 1935 to acquire the stock (Art. IX, Sec. 2, App. 34b);

(h) consummation of the foregoing transactions, together with preliminary transactions (concentration of all properties in the hands of the Inland Trustee, liquidation and dissolution of certain of the subsidiaries

of American, establishment of reserves and accounts for payment of claims, etc.) according to a specified and detailed program (Art. IX, Secs. 1, 2, 4, App. 32b, 34b, 36b).

Referring item by item to our summary of the Trustees' Plan, the Kern proposals would:

(a) Eliminate the statement of principles in the Trustees' Plan (the proposals being inconsistent with those principles) (Art. I, Sec. 2 deleted by Kern proposals, App. 5b).

(b) Eliminate the valuation on which the Trustees' Plan is based; the proposals do not state the valuation on which they are based, but refer to the Trustees' valuation and the testimony of higher valuation which was rejected by the District Court (Kern Art. V, Sec. 3, App. 20b).

(c) Eliminate any findings as to the solvency or insolvency of the Debtors (Art II, Sec. 2 deleted by the Kern proposals, App. 6b).

(d) Eliminate the unsecured borrowing of $4,000,000 from Chemical Bank and substitute three series of mortgage securities (Series A Sinking Fund Bonds, Series B Convertible Bonds, Series C Sinking Fund Note) in aggregate principal amount of $4,250,000 (Kern Art. VII, Sec. 2, App. 23b).

(e) Eliminate the provision for payment of claims by the Trustee, and substitute a provision for their payment by the New Company to be organized to carry out the Plan (Kern Art. VIII, App. 30b).

(f) Eliminate the provision for reservation by the Trustees of funds to pay Class 1 claims (including distributions heretofore ordered; and reorganization fees and expenses), and substitute a provision for the as-

sumption by the New Company of liability to pay them (Kern Art. IX, Sec. 4, App. 36b).

(g) Instead of transferring to the New Company physical properties and cash balances *after* reservations by the Trustees for payment of claims and reorganization fees and expenses, the Kern proposals would transfer all physical properties and *all* cash balances to the New Company (Kern Art. VII, Sec. 1, App. 23b).

(h) Eliminate the specified and detailed consummation program and substitute therefor a general provision that the Kern proposals are to be consummated "in accordance with" the statute (Kern Art. IX, Sec. 1, App. 35b).

Under the Kern proposals, the capitalization of the new company would have been $4,250,000 aggregate principal amount of the three series of sinking fund or convertible mortgage securities and $4,765,160 par value of common stock, or a total capitalization of $9,015,160. The Sinking Fund Bonds and the Convertible Bonds would be sold to two insurance companies and the Sinking Fund Note to a banking institution. The common stock ($4,765,160) would be (a) issued to public holders of Kentucky Bonds and Debentures ($3,265,160), (b) offered for sale to such holders ($694,650), and (c) sold outright to the underwriters ($805,350). The underwriters also would have purchased from holders of Kentucky Bonds and Debentures, at par, such of the common stock received by such holders under (a) or offered to them under (b) as the holders wished to sell or did not desire to purchase, respectively. An additional $470,000 par value of stock would be reserved for conversion of the Series "B" Convertible Bonds. Fees and expenses of the purchasers of the Sinking Fund Bonds, the Convertible Bonds and the Sinking Fund Note (including counsel fees) would be paid by the new company upon con-

summation of the Kern proposals. Liabilities for priority claims would be assumed by the new company. In the case of Columbia's claims, payment would be made "as funds become available" after completion of appellate review of proceedings on the Kern proposals. The amount then to be paid to Columbia would be equal to the principal of and accrued interest on its Bonds and Debentures claims against Inland and the principal of its unsecured claims against Inland. Nothing would be paid to Columbia on any of its secured and unsecured claims against American or on the Kentucky Bonds and Debentures held by it.

Considering the nature and extent of these proposed changes in the confirmed Plan, it plainly was not an abuse of discretion for the courts below to conclude that the Kern proposals were a new plan, and to refuse to begin the series of hearings and other procedures with respect to them.

3. Petitioners' Contentions

As regards this ground of the decision below, the attack of the Petition is directed solely at the principle applied by the District Court and the Court of Appeals. The main argument* is that by enactment of Section 229c in 1952,

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*The Petition includes several subsidiary contentions which can be disposed of rapidly. The substance of all of them is that the Court of Appeals erroneously believed that permissible changes in a confirmed plan do not include "changes of a material character", but only changes in "mechanical details" (Petition, pp. 13, 18). This argument is a straw-man. The statements of the District Court and the opinion of the Court of Appeals show that each court (i) recognized that the court had discretion to approve changes which materially and adversely affect creditors, (ii) cited as authority decisions holding that the court has such discretion (*Country Life, Knight* and *Prudence-Bonds*), and (iii) reached its decision, not because of any one of the "changes of material character" proposed by Kern, but because the cumulative effect of all such changes was a *plan*, not depending on anything in the confirmed Plan, and requiring still another series of hearings and proceedings covering the *entire* range of matters of which Chapter X requires consideration.

Moreover, the Petition, while quoting from *Collier* with respect to changes in a confirmed plan, gives no intimation that the editors

Congress took away a District Court's discretion to reject reorganization proposals offered after confirmation of a plan, and *required* it to start new plan proceedings on *any* reorganization proposals—even a new plan—so long as offered prior to "substantial consummation" of the Plan, as defined in Section 229a.

This argument is frivolous. Neither the terms of Section 229* nor its legislative history gives any indication that Congress intended to uproot the well-settled law that proposals to change a confirmed plan are addressed to the discretion of the court and that sound discretion requires the rejection of proposals which are a new plan. By its terms, Section 229 fixes the point in the reorganization proceedings *after* which the District Court does not have discretion to consider *any* "alteration" which materially and adversely affect the interests of creditors. It fixes as such point the "substantial consummation" of the confirmed plan. Section 229 does not purport to state anything with respect to the discretion of the District Court, *prior* to "substantial consummation", to refuse to entertain new reorganization proposals.**

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of *Collier* fully support the principles applied by the courts below, *viz.*:

> "Once a plan has been initially approved by the judge under Section 174, the opportunity has passed for proposals of new plans as such, unless the approved plan is rejected by the creditors or stockholders or fails of confirmation. Proposals submitted after approval, therefore, may be only in the nature of alterations or modifications of the approved plan.
>
> "...
>
> "All proposed changes require the approval of the district judge, and whether or not they will be incorporated in the plan rests in the exercise of his discretion which will not be reversed by an appellate court except for abuse thereof." (6 Collier, Bankruptcy, 14th Ed. § 11.11 pp. 3898-3899.)

*Section 229 is quoted in full at Pet. App. 3c.

**The purpose of Section 229 was explained in the Committee reports as follows:

> "Section 24 of the bill adds a new section 229. This section will clarify the present uncertainty as to the point in the

B. Refusal to begin new plan proceedings on the Kern proposals does not conflict with the decision of the Second Circuit in *Knight* v. *Wertheim*.

The Petition urges a conflict between the decision of the Court of Appeals and that in *Knight* v. *Wertheim*.** But consideration of the facts and opinion in that case shows that there is not such a conflict; and further that, as to the single question in this case to which *Knight* is relevant, the Court of Appeals applied the same principles which Judge Learned Hand stated and applied in *Knight*.***

The Facts in Knight

The debtor owned the Equitable Office Building in lower Manhattan. Proceedings under Chapter X were instituted April 10, 1941. The trustee filed a plan of reorganization February 24, 1944, various amendments were proposed from time to time, the plan was "approved" December 4, 1945, and "confirmed" May 13, 1946. There were not any appeals in the plan proceeding or from the confirmation order. Two months after confirmation, stockholders filed a petition which proposed an alteration of the confirmed plan.

The *plan* provided that Equitable's First Mortgage Bonds ($16,000,000) would remain outstanding undisturbed and its Second Mortgage Bonds ($3,000) would be paid in cash. Equitable's old debentures and old common stock would be treated as shown in the following tabulation:

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reorganization proceeding at which rights vest under the plan sufficiently to make it equitable to cut off *further right to amend or modify* the plan as to matters materially and adversely affecting the rights of creditors or stockholders." (House Report No. 2320 (June 26, 1952) accompanying S. 2234 (82d Cong., 2d Sess.).

**158 F. 2d 838 (2d Cir. 1946).

***The opinion of the dissenting judge does not refer to *Knight* or state a position based upon it, even though Petitioners argued at length to the Court of Appeals that the decision of the District Court was contrary to *Knight*.

Securities of the Debtor	Common Stock in the New Company
Old Debentures	
($4,754,000 principal plus $1,188,000 accrued interest)	
To be exchanged under the Plan for:	
(a) $2,852,400 New Income Bonds convertible for two years into 456,384 shares New Common Stock.	(a) 456,384
(b) 475,400 shares New Common Stock.	(b) 475,400
Old Common Stock	
(862,098 shares)	
(c) To be exchanged under the Plan 1 for 10 for 86,209.8 shares New Common Stock.	(c) 86,209.8
Total shares of New Common Stock upon conversion of New Income Bonds.	1,017,993.8

The *alterations* proposed by stockholders were: to sell pursuant to an offer of City Investing Company (a large real estate company) all of the shares of new Common Stock in items (a) and (b) above (earmarked under the Trustee's Plan for the old Debentures) and with the monies so raised, together with the debtor's liquid assets, to pay off the old Debentures' principal and interest. The provisions as to shares of new Common Stock, item (c) above, would remain as before, *i.e.*, those shares would be issued, 1 for 10, in exchange for shares of Old Common Stock. Old Common Stockholders would have a right to subscribe for the shares of new Common Stock in items (a) and (b) (except for 69,686 shares to be received as a commission by City Investing Company under its offer). The new Con-

vertible Income Bonds would be eliminated from the plan. No other change in the trustee's plan was proposed.

The District Court rejected the proposal on the ground that its confirmation order ought to be final.

The Decision in Knight

The Second Circuit reversed this decision. The quotations from Judge Learned Hand's opinion set forth above (pp. 21-22) reflect the principles which it applied with respect to the stockholders' proposal to alter the confirmed plan—*viz.*, that (i) such proposals are addressed to the discretion of the court, to be exercised upon consideration of "the whole nexus of facts", and (ii) discretion should be exercised against proposals which require changes in the confirmed plan "so radical" that they amount in substance to a new plan. Clearly, there is not any conflict between these principles and those applied by the Court of Appeals in this case, which it stated as follows:

> "We think the district court did not abuse the discretion expressly granted him by the statute; but, on the contrary, we consider that he used sound common sense, practical judgment in declining to permit an altogether new plan to be submitted, under the guise of alterations and modifications, in lieu of a sound plan already confirmed by him and approved by this appellate court, with certiorari denied by the Supreme Court of the United States."

Neither is there a conflict with respect to the decisions that the proposal in *Knight* was not a new plan but that the Kern proposals are. The statement of the *Knight* plan and "alterations" above shows the limited scope of the "alterations" proposed in *Knight*, and the *Knight* opinion expressly relies upon the limited scope of the "alterations".*

*In rejecting the argument that the stockholders' proposals were a new plan, Judge Hand stated:

The *Knight* "alterations" did *not* involve, as did those proposed by Kern, (i) the issuance of classes of securities not provided for in the plan, (ii) changes in the amounts of securities provided for by the plan, (iii) changes in the property to be transferred to the reorganized company, (iv) changes in the method of payment of claims, (v) elimination of the consummation procedures set forth in the plan. Neither did they involve, as did the Kern proposals, the elimination of plan principles, the elimination of findings of insolvency, a new valuation, and the redetermination of substantive rights of creditor classes. In view of these facts, the statement in the Petition that "if the alterations presented in this case constitute a 'new' and 'completely different plan', this was no less true in *Knight*", is preposterous.

Petitioners refer frequently (Pet. 11, 12, 21) to Mr. Justice Reed's opinion granting a stay in the proceedings which eventuated in the *Knight* decision, *viz.*, *In re Equitable Office Bldg. Corp.*, 72 Sup. Ct. 1086 (1946, not officially reported). Mr. Justice Reed in that opinion also emphasized that the proposals there did not basically alter the trustee's plan, stating at p. 1089:

> "Under the stockholders' present proposal they would receive immediately the *same* number of

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> "... Nor were the proposed changes themselves so radical as to fall within our decision in Country Life Apartments v. Buckley, supra. The first mortgage was *to remain as before*; the balance upon the second mortgage was to be *paid as before*; a new corporation was to be organized with the *same* capital as before; the old shareholders were to have the *same* number of new shares as before; the current liabilities were to be *paid as before*. The *only change* was that the debenture bonds were to be paid in cash instead of refunded in new bonds and new shares, and that to do this the shares which had been reserved for them, either immediately, or to answer their conversion privilege, were to be sold to the old shareholders, taken up by the City Investing Company, or were to go to that company for its underwriting commission." (158 F. 2d at 843)

shares as under the trustee's plan. The reorganization corporation would have the *same* number of shares. 862,096 of the shares allotted the present debenture holders would be taken by the underwriter at $6 per share. This money and corporation cash would pay all debts and expenses. If the value of the property remains at $21,375,000 the book value per share would be the *same*."

CONCLUSION

The Petition for Writ of Certiorari (No. 809) should be denied.

Respectfully submitted,

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April 19, 1960.

APPENDIX

Some Comments on the Excerpts from the Address by J. Arnold Pines, Appendix C to Petition

Mr. Pines stated at the outset of his address* that "his area of responsibility, as Chief Financial Analyst of the Division of Corporate Regulation of the SEC, extends to three statutes", one of which is Chapter X of the Bankruptcy Act. Accordingly, his address expresses views on a matter still in litigation lying squarely within his area of responsibility at SEC, namely, the proceedings in which the Petition now seeks certiorari. Mr. Pines' address expresses a point of view which counsel for the SEC, as well as counsel for the Petitioners, had urged to the District Court and the Court of Appeals, and which, when he delivered the address, had been rejected by both Courts.

We do not object to Mr. Pines expressing to the Rutgers Business School his dissatisfaction with court decisions adverse to his views in his official position. Considering, however, that the Courts below have rejected such views, for the Petition to treat Mr. Pines' view as some sort of authority seems to us bizarre.

We limit our comments below to those statements in Mr. Pines' address which concern valuation.

I.

". . . the Inland estate increased in value far beyond expectation, . . . " (Pet. App. 24c.)

This refers to the fact that the 1969 stock market valuation, derived from the capitalization envisaged by

*Mimeograph made available by SEC, p. 1 (not included in the Kern Petition's excerpts).

Kern's proposed underwritings, was higher than the reorganization value as of December 31, 1957, which was based on discounting future earnings and was found fair by the District Court in the spring of 1958 (affirmed by the Court of Appeals).

This is measuring one kind of valuation against another.

If one limits the inquiry to a comparison of stock market valuations, that involved in the Kern proposals should be compared with the stock market valuation made by Kern's expert witness in the hearings on the Trustees' Plan.* Comparing these two, there was a substantial *decrease* (not an increase) between 1957 and 1959 in stock market value. (Mr. Pines' address does not refer to the earlier stock market valuation.)

If one limits the inquiry to reorganization value based on estimates of earnings, it is known that actual earnings for calendar year 1958 (*i.e.*, the year between the date of the Trustees' valuation (as of December 31, 1957) and the 1959 Kern proposals) were substantially less than earnings for the year 1957, and that total revenues were substantially *less* than those estimated by the Trustees' expert as a basis for the Trustees' valuation.** There was, of course, a

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*Appendix to Brief of Appellant Paul E. Kern is the United States Court of Appeals for the Sixth Circuit, September, 1958 (Nos. 13657, 13660), filed as part of the record before this Court in Paul E. Kern, *Petitioner*, v. The Columbia Gas System, Inc. et al., *Respondents*, No. 766, October Term, 1958, pp. 134a-172a.

**Detailed Analysis, Inland Gas Corporation, by L. E. Kihlken, February 13, 1958, filed as part of the record before this Court in Paul E. Kern, *Petitioner*, v. The Columbia Gas System, Inc., et al., *Respondents*, *supra*.

The Trustees' 1958 earnings reports are not in the record here; however, they were in the record before the District Court and the Court of Appeals, and these reports were summarized in our brief to the Court of Appeals. We do not know whether Mr. Pines, as Chief Financial Analyst, was familiar with this brief, but counsel for Petitioners obviously were.

substantial increase in the Trustees' cash during the period between the December 31, 1957 Trustees' valuation and the Kern 1959 proposals; this would naturally result (and it was foreseen that it would result) in some increase in reorganization value, although not exactly equal in amount to the increase in cash.

II.

> "... the valuation submitted on behalf of the Trustees' plan was more than $3,500,000 less than the amount at which sophisticated institutional investors and underwriters, only one year later, agreed to purchase the enterprise. ..." (Id.)

The "only one year later" phrase is an inaccurate description of the period between the Trustees' valuation and the submission of the Kern proposals. The Trustees' reorganization valuation was as of December 31, 1957; the Kern proposals were submitted in May 1959 and specified as their target date August 31, 1959 (which Mr. Pines himself, on an earlier page, has recognized as the date of the stock market valuation, Pet. App., 23c). Even as of that date the Kern stock market valuation counted on the advantage of postponing for a substantial, though indefinite, period many of the obligations which the Trustees' Plan regards as obligations for which a plan should make immediate provision.

In a reorganization such as this, in which cash generation from trustee's operations is about $1,000,000 for each year reorganization is delayed, it obviously makes a substantial difference that the period between the Trustees' valuation and the Kern stock market valuation was 20 months, rather than the 12 months stated by Mr. Pines. But even more important is the fact that "sophisticated institutional investors and underwriters" did not (whatever

the elapsed time) "agree to purchase the enterprise". They indicated a willingness for a limited period and subject to a number of contingencies, to purchase securities of the reorganized company. In estimating value there is a necessary and obvious difference in the relative probative weights of (a) an offer to purchase the assets of a corporation and (b) an underwriter's offer to float its securities. It is the difference between (a) an offer based on stable operational factors and not on stock market fluctuations, and (b) an offer, depending on stock market conditions, made in a volatile stock market.

III.

> "We must remember that institutional investors and underwriters are not prone to throw money away, and therefore they would hardly be likely to commit themselves to purchase the securities provided for the bondholders' proposals unless they were convinced as to the value of the underlying assets." (Id., 23c.)

No doubt the two insurance companies and the bank expected that the First Mortgage (which they required as security for the new company obligations which they might acquire under the Kern proposals) would cover underlying assets adequately protecting the $4,250,000 of mortgage securities.

But that does not take us very far in proving that value has increased (as Mr. Pines asserts) from approximately $11,000,000 to $14,500,000. If the capitalization contemplated by the Kern proposals contains anything probative of an increase in value, it must be found in the underwriting of the common stock. The inferences to be drawn from investment bankers' opinions as to common stock are obviously different from those to be drawn from insurance

company opinions of first mortgage bonds. Stock underwriters purchase with an eye to the price at which they can sell. This, as most people know, takes in a multitude of considerations other than underlying asset values and other than values appropriate for reorganization purposes. Stock-market prices sometime bear little relationship to ". . . the value of the underlying assets".

We agree with Mr. Pines that stock underwriters "are not prone to throw money away"; but his "therefore" clause is to a considerable extent a *non-sequitur*.

IV.

Mr. Pines says that, since Columbia would supposedly receive only $3,021,000 in equity value under the Trustees' Plan, one must ask why it resists the Kern proposals which will yield it much more in cash. Then he asks:

> "Can it be that Columbia does not really value the system's assets at the amount urged by the Trustees and accepted by the courts, but rather at some larger amount, perhaps approximating the value embodied in the bondholders' proposals? . . ." (*Id.* 23c.)

This in effect is an old stalking horse of Mr. Kern's. As appeal has followed appeal, Kern has each time bewailed—"But the last time Columbia said that it would receive much less in equity value than it now will." This is true; as reorganization has been repeatedly delayed by further appeals, the Trustees' operations have generated additional cash and this (though not in corresponding amounts) has tended to increase values. Values in each appeal must be related (and Columbia's briefs have in each case expressly so related them) to the valuation and financial statements in the then current record. The Trustees' Plan itself recognized that values would increase through cash accumula-

tions between the date of the Plan's valuation (December 31, 1957) and the time of final disposition of appeals from an order of confirmation, *and specifically provided for the issue of stock equal to net worth at the latter date.**

As to Mr. Pines' rhetorical questions, quoted above, Columbia had given the answer—"Yes, it did believe that the value of the equity was now more than the $3,021,000 (as of December 31, 1957) on which the Trustees' Plan was based." It had given that answer a good many months before Mr. Pines addressed the question to the Rutgers Business School students, *viz.*, in Columbia's Reply Brief dated October 3, 1959, to the Court of Appeals, pp. 11 et *seq.***

*Plan, Article VII, Sec. 2, App. 23b.

**Again, we do not know that Mr. Pines, as a financial analyst, had been informed as to the contents of Columbia's briefs; but counsel for Petitioners certainly were so informed.